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## TAXATION—DISCUSSION

E. R. A. SELIGMAN: I wish to express my appreciation of the admirable way in which Professor Adams has handled a difficult subject. I appreciate the fact that he is dealing with a local situation of some unusual difficulty and I have nothing but admiration for the way in which he has endeavored to handle the difficulty. And yet, notwithstanding all this, I cannot bring myself to believe that the scheme which he outlines is advisable for the country at large, or even, in the long run, for the State of Wisconsin. The reasons why I am opposed to state income taxes may be summarized as follows:<sup>1</sup>

1. The narrower the base of the tax the more unsuccessful does an income tax become. In former times a local income tax was fairly workable, because incomes were local in character. In modern times the income of the taxpayer has little to do with the locality in which he happens to live. If, as every one concedes, a state income tax is preferable to a local income tax, it follows that a federal income tax would be still better than a state income tax. Any attempt to control national incomes by state methods does not promise much success.

2. In the second place, the conflicts of double taxation would be ever present. The combinations of multiple taxation by different tax jurisdiction are almost terrifying in their complexity. With more adequate administrative methods on the part of the states, the possibility might become a reality. In Germany state income taxes are possible because of the federal law governing the subject. In this country such a law does not and probably cannot exist.

3. The third consideration is that of administrative efficiency. Federal administration is far more effective than state administration. Not only is it easier to secure expert assistance for the larger problems involved in national affairs, but the contact between official and citizen is not so likely to have that unfortunate relationship which will exist in the smaller administrative sphere.

4. Finally, fourthly, the adoption of a state income tax would embarrass state finances. If the states took the income tax, the federal government would be likely to take the corporation and

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<sup>1</sup>They are set forth in detail in Seligman, *Income Tax*, New York, 1911, pp. 642-58.

the inheritance taxes. The states which are working out the scheme of tax reform at present rely to a continually increasing extent on corporation and inheritance taxes. A state income tax, in view of the state general property tax, would thus check a salutary movement.

Any one of the above four arguments would in itself be sufficient. Taking them together, their cumulative force is overwhelming. Especially in the more advanced and industrial commonwealths a state income tax would be a step backward, not a step forward. If, however, under the name of the income tax we introduce what are either business taxes or house rental taxes, the situation is very different.

The real difficulty lies at another point. According to the arguments advanced above the income tax should be a federal tax; but from the point of view of revenue the income tax is needed for state and not for local purposes. Why would not a way out of the difficulty consist in having the tax levied and administered by the national government with an apportionment of the proceeds—to a large extent at least—to the various states, perhaps to be further apportioned to the localities? The method of federal administration and state and local apportionment is one that is familiar to students of public finance, but it has not yet been tried to any great extent in the United States. Some adjustment must be reached whereby the legitimate demands of equality and uniformity may be secured without sacrificing the ends of efficiency and adequacy. The interests of the states must at all costs be safeguarded; but the difficulties inherent in the state administration of what has become national in character must be avoided. I am afraid that Professor Adams has not taken a sufficiently long look ahead.

**T. N. CARVER:** With the general spirit and purpose of Professor Davenport's admirable paper, I am in complete sympathy. I think, however, that there are different ways of getting at the same result at which he aims. Instead of calling everything capital that is in any way a means of acquiring wealth, I should limit it to what he has called the technological instruments of production, or at least to material things, including perhaps dwelling houses that are rented for an income. But while I should include in the capital column only an inventory of such material, tangible forms of wealth, I should make another in-

ventory for the purpose of the theoretical economist; and in this other inventory, or this other column, I should set down opposite the names of the technological instruments, etc., the factors which enable the owners of the technological instruments to get income from them. In this column I should put down, for example, the disutility involved in waiting. This acts as a check upon the supply of these instruments of production, and gives them a higher marginal productivity than they would otherwise have; and this in turn gives them greater income-procuring capacity. Again, I should set down what Mr. Hawley has called the "irksomeness of risk" as another factor which limits the number of such instruments, or reduces the willingness of men to handle them. This again adds something to their income-procuring capacity. Then there are patent rights, trade secrets, and good will, which still further control or limit the supply of some of these technological instruments and give them a still higher income-procuring capacity. Finally, there are doubtless a great many fraudulent and unscrupulous practices by means of which the same owners mulct the public and still further increase their incomes.

It seems to me that this arrangement meets the requirements of the theoretical economist better than Professor Davenport's method of putting everything—technological instruments, trade secrets, and unscrupulous practices—all into the same category. His method seems to be putting very unlike things into the same class.

Now the question will next arise, which of these functions that give income-procuring capacity to the technological instruments may be regarded as productive or useful, and which not. Inasmuch as a certain amount of waiting is absolutely essential in order that the world may be supplied with tools, and inasmuch as men do not as a rule like to wait, it seems to me that we should have to agree that that part of the income which is due to that necessity of waiting may be regarded as earned. Similarly with the taking of risk: as to whether patent rights, trade secrets, good will, etc., are productive or useful, and entitle the owner to an income, may be open to discussion. I should think that it would have to be decided independently in each individual case, with the burden of proof on the shoulders of him who denies that the income from these sources is earned.

Of course all unscrupulous and fraudulent methods of business

are not only unproductive, but are positively destructive. Income secured by these means is not only unearned; it is stolen. There are many ways of classifying wealth, but from this point of view we may logically divide wealth into three classes: earnings, stealings, and findings. Incomes secured by these fraudulent methods are stolen. The attitude of the state should be one of complete hostility; there should be no compromise. All such incomes should be prevented or prohibited. On the subject of findings, however, it seems that there must be a compromise. The unearned increment of land, and inherited wealth, are the two most conspicuous examples of this kind of wealth. Though such wealth is not strictly earned, it is entirely false to say that it is stolen. It is like finding wealth; it is wealth which comes to one in a perfectly open, legal manner, recognized and approved by all modern states, and in fact by all civilized society. Only such wealth as may be classified as findings, it seems to me, is fit to be made a special subject of taxation. Stealings, as before intimated, are not fit subjects for taxation; they should be prohibited altogether. But inherited wealth, and the unearned increment of land, may very well be made special subjects of taxation; for the reason that taxes may be raised from these sources without really disturbing or repressing any productive industry. From a purely economic point of view, such taxes conform to the rule of imposing the least possible burden by means of taxation. Tax the products of industry, and you not only tax the payer but you repress industry. Tax these forms of unearned wealth, and you burden the payer, it is true, but you do not repress industry. There is, therefore, less burden imposed upon the community by this form of tax.

**H. A. MILLIS:** Professor Adams's paper is very interesting and unusually suggestive. It contains a great many things which appeal to me very strongly. The relativity of things is made to stand out clearly. Great emphasis is very properly placed upon the machinery used in the administration of a tax system. The fact is realized that the possibilities of an income tax depend largely upon the details of the law, the details of the administrative system, and the popularity of the tax itself. With all of this and much more contained in the paper I heartily agree.

Professor Adams makes "a plea to the economists of this country to cease declaring flatly that a state income tax is impossible and to formulate the conditions which must be fulfilled to make the

state income tax practicable." He has in mind certain measures and administrative methods which he believes would effect an improvement in the systems now employed in state and local taxation systems in which the general property tax occupies a dominant position. While agreeing with most of what Professor Adams has said and with his assumption that our present systems are very faulty, I wish in the few moments at my disposal merely to point out some difficulties which his scheme—in so far as he has outlined it—has not overcome.

In the first place, Professor Adams would exempt from taxation all intangible and a part of tangible personal property. In the second place, he would introduce income taxes levied under a state law, upon assessments made by local officers appointed by and responsible to a state tax commission, the rates imposed being low and prescribed by the state law. His argument calls for (1) a tax upon the incomes derived from business conducted in urban communities and presumably of a local character, without regard to the place of residence of those who share these incomes; and (2) a tax upon the entire incomes of those who reside in these urban communities, without regard to the sources from which their incomes are drawn. The habitation tax would be used as a minimum in assessing personal incomes; no doubt external indicia would be employed in assessing incomes from local business as well.

These two taxes Professor Adams advocates to make good the losses from the exemptions of personal property and to add to the revenues of the treasury, and to make for greater justice in taxation. They are preferred very properly to heavier taxes upon real estate as it is now taxed. They are also preferred to differential rates upon certain kinds of personal property, and such business or occupation license taxes as are now employed in the United States, the Canadian provinces, and many of the European countries.

In passing I may state that I fail to see why the income tax should be regarded as a substitute for the low rates placed upon a few kinds of personal property, as in Maryland, Pennsylvania, and Connecticut, unless the total of the two taxes should become greater than the traffic will bear. Logically, it seems to me that his suggested business income tax should be regarded as a substitute for business taxes levied in lump sums or graded according to gross earnings, as in Louisiana, according to space occupied or rental values of the premises used or otherwise,

while his personal income tax should be regarded as a substitute for the local habitation tax, or a federal income tax.

Professor Adams advocates the net earnings business tax because net earnings indicate ability, while gross earnings, rental values, etc., do not. All of his adverse criticism of such business taxes as are now employed on this continent is well merited. Yet I do not believe that the substitution of a net earnings base would effect an improvement. In the first place, taxpayers do not care to let their profits from specific business enterprises of a local competitive character become known; yet it would not do to keep the records of assessments and of taxes paid secret were it possible to do so. In the second place, in spite of the great improvement which is still possible in administrative methods, the opportunities for fraud and evasion would be too great and corruption would probably follow the introduction of a local net earnings tax. The appeal to the success of our various commissions in dealing with corporation accounts and corporate values carries little weight here, for these state officers have usually not been assessing net incomes for the purpose of taxation. Moreover, the problem of assessing shopkeepers and small business men generally is a difficult one, and one which offers more ways and greater inducement for evasion. It is interesting to note in a few instances in the southern states that rough business license taxes have been substituted for the income tax, because they were more definite and would work. That the delegates to the last Constitutional Convention in Louisiana eliminated the income tax long used for both state and local purposes and retained the business tax levied according to gross earnings, is not without point in spite of the fact that the latter tax is unsatisfactory and has recently been severely criticised. The Province of Ontario introduced a business tax based upon rentals a few years ago and restricted the income tax which had been more or less of a farce. Say what you will, net earnings are in most cases difficult for the *assessor* to estimate, though, as asserted in the paper, they may be easily enough reckoned by the business man, who must pay the taxes or evade them. My own feeling is that the net earnings business tax would not prove successful here, though in a modified form and under different circumstances it has proved so in Prussia. In most instances, without minima based upon tangible facts, assuming such administrative machinery as we can expect to develop, a net earnings tax would probably be a farce.

With minima established, the income feature would soon disappear and we should have a system based upon external indicia employed at the discretion of the assessors. With our attitude toward government and with all the difficulties involved, it is believed that the Ontario system of business taxes based upon rentals, with all its shortcomings, is more satisfactory than any system would be, based upon net income.

As to the personal income tax, which rests upon a different argument, several of our commonwealths have tried it without much success. We must agree with Professor Adams, however, that this failure signifies little or nothing with reference to the possibilities of an income tax levied under a law properly framed and enforced, rather than put in the form of a slight supplement to the general property tax, as it usually has been, and left to the local assessors to apply as they pleased or to ignore. Professor Adams's tax would have an independent position and it would be somebody's business to enforce it. Moreover, a strong central commission would render the local assessors and the public the great assistance which would be within its power. Use would be made of records of dividends, of interest payments, etc. Finally, the habitation tax is suggested to establish minima. All of these features are new and would doubtless cause the personal income tax to work much more successfully or much less unsuccessfully than it has in the past. Moreover, as we became accustomed to the tax, it might be more favorably regarded and the administration might become less difficult, as has been the case in Great Britain. Such an income tax could not be worse than the best habitation tax and would be much better than a poor one. It is in point to note that in France the habitation tax has generally not been imposed as provided by law, but as the assessors saw fit in their efforts to improve upon the law and eliminate some of the great injustices which would otherwise be involved. Yet, with the education we have had in tax evasion, with the slight use which can be made of stoppage at the source, with deductions and allowances which must be made to ascertain taxable income, it is doubtful whether justice would be more nearly attained than with a reasonable business tax, a heavy inheritance tax, good corporation taxes, and the taxation of the unearned increment in its various forms, without an income tax. It should be pointed out also, that the specific measure advocated by Professor Adams offers unusual facility for evasion in that it is

not to be employed in agricultural districts. With most kinds of personal property not subjected to taxation, it seems to me that every inducement, even with a low tax rate, would be given to persons whose incomes are large, to migrate to a country place, for presumably nearly all of their tangible and taxable property would retain its *situs* unchanged.

If an income tax is to be employed, it seems to me that it should be employed by the federal government. The federal government needs the revenue in case of emergency. The revenue could be used in reforming the customs system. Moreover, though the federal government is farther removed from the citizen and a federal income tax would appeal less to the taxpayer than one used by a state or local government, it can employ stoppage at the source more extensively. Finally, state income taxes would lead to migration from jurisdiction to jurisdiction just as the taxation of personal property has. Professor Adams's contention that there would be insufficient motive is not well taken, for the reduced rate of the property tax to which he refers would still apply to most tangible property left behind when a residence was changed, and if the income tax really amounted to anything its burden would undoubtedly be greater than the tax imposed upon any personal property actually assessed at a new residence gained. The income tax is for these reasons preferably a federal tax. Nor can it well serve as a source of both federal and state revenue without either causing the rates to become too high, or the receipts to be fiscally unimportant.

In expressing the opinion that the income tax (as distinguished from a business tax) is preferably a source of federal revenue, I would not be understood as advocating its use by the federal government at the present time. The federal government should have the power to employ it in emergencies. Until our conditions change materially, however, I am of the opinion that justice in taxation will be more nearly realized in other ways; and certainly revenue for the ordinary needs of the federal, state, and local treasuries can be secured with more certain results from taxes presenting fewer administrative difficulties.

MAURICE H. ROBINSON: It does not need argument to prove the feasibility of a tax on unimproved land values, when considered from the practical point of view. Land is valued for commercial purposes in the real estate market every day in many

cities and in many countries. It is also being valued by public authorities for purposes of taxation in several countries with a degree of accuracy that has been found impossible in many other lines of properties. If such taxation is unconstitutional, even constitutions may be changed whenever public opinion demands.

The question of land taxation then may be considered upon its merits, that is, its effects upon the social welfare. It is often affirmed, that the land is the free inheritance of society, and, therefore, that its income as such belongs to all in their associated capacity. That this was the original condition may be admitted without in any way affecting the assertion that such is not the condition today. Almost without exception the larger proportion of the land originally held by the government has been transferred to individuals, with one reservation only, namely, the right to take a portion for public uses, or all on proper compensation. Without breaking faith with the present holders, therefore, the unearned increment accumulated in the past, must be left in private hands. No guarantee has, however, ever been made that the present proprietors may remain in possession of the future unearned increment. Why, then, should they be permitted to reap, it is asked, where they have not sown.

It may be observed, in the first place, that a portion of the rental value of land is due, not to locations or to intrinsic fertility, but to certain conditions contributed by those who are living in the particular locality. Such value, while socially created, is not created by the city as a political unit, or by the state. To whom, then, should the income accrue?

In the second place, an increase in land values may be caused either by the increase in population within certain limits, as, for example, New York City, or by an influx of population from outside the boundary. In the former case, the enhanced value from the economic standpoint belongs to the city. In the latter case, before the city can justly claim the increase in value, it must compensate those other communities that suffer a corresponding loss. The above cases are cited not to prove that the taxation of land values to the full extent of the annual increment is undesirable, but to show that such action must be justified, if at all, upon social rather than economic grounds. When the problem is considered in this light, certain questions arise of which the following are particularly relevant.

1. If the annual increment in land values is taken annually by

society, shall the unearned increment in other lines be permitted to remain in private hands?

I shall pass over this point with the observation that while I am unable to agree with Professor Davenport's conclusions as to the extent of the unearned increment in other fields, I see no reason for taking one class and omitting the others, provided they are all equally permanent.

2. If confined to land values, should the increase in all values be taken or only those arising from superior location?

Agricultural land in this country is, as is well known, generally held by those who cultivate it, while city land on the other hand is quite generally owned by absentee proprietors. As a result, the economic rent of agricultural lands is being fairly evenly distributed among the agricultural population. If owing to fundamental economic laws or unwise social regulation the bulk of the agricultural lands show a tendency to become concentrated in the hands of a few, a new problem will arise, which may well be left for the future to solve.

In the second place, it is now generally recognized that soil, contrary to the opinion formerly held, is subject to rapid deterioration and rapid exhaustion, unless the constituent elements taken by the crops are replaced by some form of plant food. The owner who cultivates his own land has every incentive to maintain its fertility. The renter, unless actuated by higher social ideals than those which usually prevail, has an even stronger incentive to wear the soil out within the period during which he occupies it. Location values, on the other hand, are not subject to this kind of depreciation, and consequently their taxation would not result in the waste of the social capital.

In addition to the location and soil values, there is a third division of great importance, namely, the mineral deposits. Owing to their adventitious character and the fact that they can be successfully exploited only by large aggregations of capital, mineral wealth, above all other objects, is a fitting subject for public ownership or taxation to the full extent of the unearned increment.

3. Shall all the increased value thus arising be taken annually by the state, or shall it become a joint landlord with private owner?

It may be found well worth the while of theorists and of the public authorities to consider the profit sharing principle in this

connection. Society as a whole has a large share in creating the so-called unearned increment in land values. On the other hand, the intelligent utilization by individuals of both location and fertility value, is a factor not to be neglected. A sharing of the annual income arising from these sources may prove of large practical importance in solving this problem, by giving the state a larger income to use for educational and other purposes, while at the same time furnishing a sufficient incentive for maintaining a widely diffused individual ownership in land.

4. And finally, may not the state, by social regulation, universal education, improvements in transportation facilities, sanitary and housing conditions, and possibly the limitation of the amount of land that may be held by one individual or one organization, together with the policy of assisting individuals to become proprietors of a small portion of the land, accomplish the objects aimed at by the advocates of land nationalism, without assuming burdens that seem impracticable, if not impossible, under present social, economic, and educational conditions?

The field of social regulation, of public education, and improvements in transportation facilities in the interests of social welfare, is as yet, almost untouched. Every improvement in transportation, whereby persons and products are more cheaply and more expeditiously moved from place to place, is a powerful force in leveling location values, and thus diminishing the unearned increment arising from this source. A system of universal education would destroy many kinds of the predatory unearned increment. The improvement of public health and of public sanitation would in themselves remove many others; and consequently, with an enlightened and healthy citizenship, social regulation would have a much less serious problem than under present conditions.

The above considerations, together with others of equal significance which might be added, lead to the following conclusions:

1. No program of economic reform founded upon the basis of sharing the unearned increment, arising from ignorance, helplessness, fraud and treachery, unsanitary conditions of a public nature, special privileges not granted by the state, monopolies, etc., between the recipients and the state through taxation, can for a moment be defended from either the economic or the moral point of view.

2. Wherever the unearned increment is due to permanent and

fundamental natural and social conditions—as, for example, mineral deposits, locations, and the like—some form of taxation, or more exactly joint landlordship, is not only advisable from the viewpoint of public revenue but is indispensable for the purpose of preserving even a reasonable standard of equity in distribution.

R. B. BRINSMADE: I wish first to pay a tribute to the frank and very able paper of Professor Davenport. I only wish that his paper, along with the supplemental criticisms of Professors Carver and Robinson, could be published in every trade-union paper of the United States, for I feel sure it would do much to counteract, in trade-union circles, the distrust of professional economists as helpers in the great movement for social reform and industrial equity. Professor Davenport, however, is evidently unfamiliar with the practical proposals of the single-taxers in his inference that they consider chiefly agricultural land values. Such a rendering, I believe, has no basis even in "Progress and Poverty", and if one reads "Natural Taxation" and the "A. B. C. of Taxation", the works respectively of T. G. Shearman and C. B. Fillebrown, the practical textbooks of the reform, the mistake is yet more evident.

Single-taxers propose to raise revenue from land value alone, but as they include in their term "land" not only farms but forests, mineral deposits, town sites, and public utility franchises (for the use of land and waterways and resources), I believe they cover all the sources of Professor Carver's "findings" (or legitimate unearned increments) except patents. The practical method of assessment of these various types of land value is suggested in my article entitled "Natural Taxation of Mining and Timber Land", published in *Conservation* for May, 1909, and in the *Mining World* for November 20, 1909.

The gains from monopolistic patent rights can be justified as both a return to the inventor for his brain work and as an inducement for him to record, for the benefit of society, his discovery, which, if kept secret, might otherwise die with him. On this basis undoubtedly our patent law has been abused, but it can be easily amended at any time to make it conform to practical justice. Land rent, however, on the other hand inevitably arises in any competitive society, and the only question before the social reformer is, who shall be allowed to absorb it? Shall it

all go to society or shall individual land holders get the whole or part of it? If one had heard today only the paper of Professor Adams and its criticism, he would have thought that taxation was a mere matter of fiscal adjustment. When one considers, however, that our present national and local governments spend about two billion dollars annually or at least one tenth of our total wealth production, it may be seen that taxation has become probably the chief factor in deciding how wealth shall be distributed among the different classes of society. Professor Davenport thinks that a direct land-value tax might be a social danger, but could anything be more demoralizing than our present indirect national taxation? In the many communities in which I have resided, the idea of the average voter of the chief purpose of a federal congressman is that he should act as a sluiceway to divert the stream of national expenditure into his local community. Would there be such a pressure on a congressman for public buildings, river and harbor works, pensions, etc., if his constituents understood that they were paying for them? Now, most voters think that a national grant is like money from home or a legacy from grandmother.

How the single tax would alter for the better the development of our natural resources can only be appreciated by a practical producer. For fifteen years I have been in practice as a mining engineer in many countries. I have been everywhere astounded that our laws still permit land-gamblers to hold up would-be developers to an extent now feasible in few foreign states. The conservation movement is but the first step toward the restoration of our land to the people. The long tolerance of present taxation absurdities by our producers is due to their ignorance of economic science. When the significance of Professor Davenport's paper becomes once known generally, there will be some fur flying among speculators, monopolists, and their dupes and lackeys.

As to Professor Robinson's idea that society has a right only to the future unearned increment, I wish to dissent. It is probably true that it would be impractical to recover the land rent paid in the past, but the recovery of that to be paid in the future (which is capitalized as the present selling value of land) is quite a different matter.

The abolition of the private appropriation of economic rent is analogous to that of chattel slavery. The latter was abolished in Brazil, without money payments to slave owners, by the de-

vice of gradual emancipation during a generation. In the same way, Mr. Fillebrown proposes to increase the land value tax 1 per cent annually for thirty years, while decreasing other taxes proportionately. This would suffice to throw the whole burden of government upon land values, raising the 20 per cent of rent now absorbed by taxation to the 50 per cent required for the whole expense of government. This would still leave 50 per cent in the hands of the land holders, which might be considered partly as a commission for rent collection, partly as a bonus for the risk of land development, partly as a margin covering incorrect assessment, and partly as a reserve available for society, through additional taxation, in case of sudden emergencies like earthquakes, famine, pestilence, or war. It is probable that all rent, beyond that needed to cover the actual requirements of the last paragraph, will gradually be absorbed by the future single tax society to cover the increased expenses of a developing social integration.